Office of Health Plan Administration
P.O. Box 720724
Sacramento, CA 94229-0724
(916) 795-2515; FAX (916) 795-4105

August 15, 2006

AGENDA ITEM 7

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

I. SUBJECT: Second Reading: Long-Term Care Program 2005 and Earlier Rates − Proposed Mitigation Strategies

II. PROGRAM: Health Program

III. RECOMMENDATION: Information Only

IV. ANALYSIS:

Staff and the Long-Term Care Advisory Committee (Advisory Committee) met on July 18, 2006 to continue discussions regarding appropriate responses to the deficit position for the Long-Term Care Program (Program). United Health Actuarial Services, Inc., the Program's consulting actuary, provided additional analysis and recommendations to the Advisory Committee (Attachment 1) to explain the proposed mitigation strategy that was presented to the Board at the June 2006 Health Benefits Committee meeting. The staff proposal for a mitigation strategy remains unchanged from the material presented to the Board at that meeting.

The staff proposal was based on the following assumptions:

- CalPERS does not have the ability to subsidize this Program with other business lines or financial reserves as does other long term care insurance carriers.

- The Program began at a point in time where the Long-Term Care insurance marketplace was relatively new and volatile.

- The long term care marketplace has matured with many insurers leaving the market; the ones that remain, or are entering the market, are savvier and more financially stable.

- In recent years, new policy sales for this Program have been low but generally better than in the individual long term care marketplace. New policies have balanced departures with total policies-in-force remaining basically flat. Based upon this, the Program cannot look to expand to cover the projected deficit.

- The CalPERS Board has approved two concepts to change the focus of the Program; 1) build reserves and no longer have a “break-even” Program, 2) do not continue to cross subsidize across products.

- In order for CalPERS to compete on a level field with commercial carriers, it would require a segmentation of the current risk pool through two-party discounts (spousal), prime, average, and sub-average rates and other discounts and incentives linked to more restrictive underwriting.

- An expansion of market penetration (new sales), would require a substantial commitment of additional assets including a real sales force (an agent network) as opposed to the marketing currently undertaken by the Program.

Staff Recommendation

Based on the history of the Program and the facts uncovered through in-depth research and discussion, staff recommends that the Program focus on ensuring there are adequate reserves to meet the demands of current in-force policies. Staff and the Consultant propose a premium rate increase (included in Attachment 1) for all 2005 and prior policies which would be self sufficient within each individual product cell to support the development of a comprehensive mitigation plan. The proposed rate increase is based upon the 2006 rates or a 20% increase, whichever is less, with the exception of “lifetime” policies which will be increased to an appropriate pricing level. This increase is to be adequate enough to build reserves with no cross subsidization for either plan design or age group. This proposal builds reserves without placing an unfair cost burden or disincentives for younger or newer policy holders. With this rate increase, members will be allowed a one-time opportunity to choose between two options as an alternative to the rate increase:

1) The member can step back to a lower Daily Benefit Allowance (DBA), (with a waiver of the underwriting requirements and utilization of their age at issuance into the Program), or

2) The member can step back from the “lifetime” policy to a six-year (or shorter) term policy (with a waiver of the underwriting requirements and utilization of their age at issuance into the Program).

Claims experience for this program and broader industry information indicate that for most members a lifetime policy represents an unnecessary cost and over-insurance. Overall, the implementation of this rate increase will bring in-force premium rates in-line with 2006 rate levels.

Staff further recommends that this premium increase become effective on February 1, 2007 or the next available billing date for those members that are not billed on a monthly basis.

As requested by the Advisory Committee, the Program's consulting actuary has provided rate increase scenarios that would be based on the following assumptions:

- A 3 percent reserve margin for all in-force policies (retaining a 10 percent margin for new policies)
- Spreading of rate increases across one through 5 years
- Continuation of the age adjustment (socialization) of a rate increase used for the 2003 rate increase
- The age adjustment should be modified to narrow the range of adjustment and provide a higher minimum rate increase than occurred in 2003

In addition, staff has attached a comparison of the proposed new rates (for 2006 as approved by the Board, and the 2005 and earlier rates after adjustment based on the proposed rate increase) and rates available in the commercial market for similar coverage (Attachment 2). The assumptions used to estimate these rates are shown as Scenario 1 in Attachment 1. On an individual basis, the Program's rates generally remain competitive, but any pricing advantage tends to erode when the discounts available from other commercial carriers are applied.

The Advisory Committee indicated that it remains uncomfortable with supporting the proposed mitigation plan based on the information provided to date. Instead, at the August 15, 2006, Health Benefits Committee, the Advisory Committee will provide the Board with an alternative recommendation requiring that no additional action on any mitigation strategy be taken until a "second opinion" or parallel valuation is completed based on June 30, 2006 policies in force. The second opinion would be completed by an actuary selected and managed by the Office of Audit Services. United Health Actuarial Services would also complete an annual valuation based on the June 30, 2006 data and the results of the two valuations will be compared and reconciled as necessary. These results would then serve as the basis of any necessary mitigation strategy that would be presented to the Board for action at a future Board meeting.

Richard J. Krolak, Chief
Office of Health Plan Administration

Terri Westbrook
Assistant Executive Officer
Health Benefits Branch

Attachments